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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1970 70-180

No. ~~1722~~

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, *Petitioner,*

vs.

UNITED STATES OF AMERICA, *Respondent.*

PETITION FOR A WRIT OF CERTIORARI to the United States Court of Appeals for the Ninth Circuit

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No.

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION,
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vs.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
to the United States Court of Appeals for the Ninth Circuit

Petitioner Bank of America National Trust and Savings Association respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered in this proceeding on February 22, 1971.

OPINION BELOW

The opinion of the Court of Appeals, not yet reported, appears in the Appendix hereto (App. i).

The opinion of the District Court for the Northern District of California is reported, 288 F.Supp. 343 (1968), and appears in the Appendix hereto (App. iv).

JURISDICTION

The judgment of the Court of Appeals for the Ninth Circuit was entered on February 22, 1971, and this petition for certiorari was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C.A. §1254(1).

QUESTIONS PRESENTED

1. Whether indorsements of six Treasury checks by a third party in the name of the named payee are effective if an agent or employee of the maker and drawer United States has supplied it with the name of the payee intending the latter to have no interest in the checks.

2. Whether the federal common law to be applied under the rule of *National Metropolitan Bank v. United States*, 323 U.S. 454 (1945), is the federal law drawn from the general commercial law as it existed in 1942, or a federal law ascertained by analogy to

Section 3-405(1)(c) of the Uniform Commercial Code, adopted by all but one of the states.[1]

STATUTORY PROVISIONS INVOLVED

Uniform Commercial Code, Section 3-405(1):

An indorsement by any person in the name of a named payee is effective if

(a) An impostor by use of the mails or otherwise has induced the maker or drawer to issue the instrument to him or his confederate in the name of the payee; or

(b) A person signing as or on behalf of a maker or drawer intends the payee to have no interest in the instrument; or

(c) An agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest.

STATEMENT OF THE CASE

The case was tried on an "Agreed Statement of Facts" prepared by counsel for the United States of America (hereinafter called United States) and Bank of America National Trust and Savings Association (hereinafter called Bank of America) and set forth

[1]The Code has also been adopted in the District of Columbia and the Virgin Islands. Louisiana, the only state which has not adopted the U.C.C., follows the same rule under the amended version of Section 9(3) of the Uniform Negotiable Instruments Act.

in the District Court opinion (App. v). These facts may be summarized as follows:

This is a padded payroll case. Six Treasury checks amounting to $6,672.00 were issued as a result of a fraudulent scheme on the part of Ronald W. Reed and John R. Sherrett, two enlisted personnel assigned to the Disbursing Office of the USS Coral Sea. A third enlisted man, Gary W. Spiller, was also assigned to USS Coral Sea and was discharged January 1, 1966. Spiller had no knowledge of the facts hereinafter stated until he was advised of them by the FBI, subsequent to their occurrence.

After Spiller's departure from USS Coral Sea, Sherrett surreptitiously obtained Spiller's identification card and inserted his own photograph in place of Spiller's. Thereafter, Reed made up all the documents necessary for the issuance of checks to Spiller, including pay records, pay receipts, check records and typed unsigned Treasury checks payable to Gary W. Spiller. The various documents were presented to the Disbursing Officer, one Ensign James Lipsett, on both regular and special payrolls; the Disbursing Officer signed the checks and returned them to Reed or Sherrett, to give to Spiller.

At all times, Reed and Sherrett intended those events to occur, which did in fact occur; that because of the operation of their conspiracy as herein set forth Spiller would not receive any proceeds of the checks. Both Reed and Sherrett were known personally to Lipsett and Lipsett had no reason, from their past conduct, to believe that they had misbehaved in

any way in their duties. It was their regular and authorized job to prepare the documents described in the regular course of business for regular and special payroll.

At the signing of each and all of the checks, Ensign Lipsett intended to pay, on behalf of the United States, a definite living person then stationed on board the USS Coral Sea to whom the money was lawfully due. The individual presenting the checks, either Reed or Sherrett, represented to Lipsett on the occasion of signing some of the checks that Spiller had reenlisted. Spiller was not known personally to Lipsett; however, on the regular payroll the name appeared with other names personally known to Lipsett. Had Lipsett known the true facts in this matter, he would not have signed the checks.

Following issuance of the checks, Sherrett signed the indorsement of Gary W. Spiller thereon, and presented them at various times at various branches of Bank of America. On each occasion the identification card was exhibited to the tellers, who did not observe any reason to suspect Sherrett. Upon receipt of payment, Sherrett and Reed split the proceeds.

Bank of America indorsed each and all of said checks with an express written guaranty of prior indorsements and presented them to the Treasury through the Federal Reserve Bank. Payment was made by the United States on each of said checks to Bank of America. Said payment was made without knowledge of the unauthorized signature of Gary W. Spiller; if said knowledge were had by the United

States, payment would not have been made. If payment had not been made, Bank of America would have made claim against the United States, alleging itself to be a holder in due course.

At the time of these transactions, all but five states had adopted the rule that the drawer bears the loss. Shortly thereafter, the remaining states adopted that rule.

The United States brought this action against Bank of America to recover the amounts paid on said checks. Bank of America filed a third-party complaint and had default judgment against Sherrett and Reed.

The trial court sitting with a jury had jurisdiction under 28 U.S.C.A. §1345.

The District Court entered judgment in favor of the United States. The Court of Appeals affirmed. Both decisions rested on *National Metropolitan Bank v. United States,* 323 U.S. 454 (1945).

In a separate criminal action, Ronald W. Reed and John R. Sherrett were convicted upon their pleas of guilty to uttering and publishing as true a falsely made Treasury check. Sentence was suspended as to both defendants, and each was placed on probation and ordered to make restitution through the Probation Office only, to the person entitled thereto, in the sum of $1,166.00, individually. No part of said sums have been paid, except $100.00.

REASONS FOR ALLOWING THE WRIT

1. THE DECISION BELOW RAISES IMPORTANT QUESTIONS OF FEDERAL LAW CONCERNING THE EFFECTIVENESS OF INDORSEMENTS OF TREASURY CHECKS.

The Court of Appeals for the Ninth Circuit affirmed judgment for the United States on authority of *National Metropolitan Bank v. United States,* 323 U.S. 454 (1945). That case, factually similar to the case at bar, followed *Clearfield Trust Co. v. United States,* 318 U.S. 363 (1943), in holding that the rights and liabilities of the government which stem from the issuance of its commercial paper are governed by the application of federal rather than local law; and that in the absence of an applicable Act of Congress, federal courts must fashion the governing rules. 323 U.S. at 456. The federal law applied in the *Metropolitan Bank* case was drawn from the then general commercial law—that a forged indorsement was wholly inoperative and gave no right to enforce payment—which was stated to be "*almost* unanimously accepted by state and federal courts" (emphasis added). 323 U.S. at 457, citing *Washington Loan & Trust Co. v. United States,* 134 F.2d 59 (D.C. Cir. 1943). In *Washington Loan & Trust,* the Court pointed out that some jurisdictions followed a different rule under the amended version of Section 9(3) of the Uniform Negotiable Instruments Act. 134 F.2d at 63, 64.

It was the need for uniform treatment of federal commercial paper that dictated a choice of a "federal rule designed to protect a federal right." *Clearfield*

Trust Co. v. United States, 318 U.S. at 367. As stated in that case:

> "The issuance of commercial paper by the United States is on a vast scale and transactions in that paper from issuance to payment will commonly occur in several states. The application of state law, even without the conflict of laws rules of the forum, would subject the rights and duties of the United States to exceptional uncertainty. It would lead to great diversity in results by making identical transactions subject to the vagaries of the laws of the several states. The desirability of a uniform rule is plain." *Id.*

The federal rule designed to protect a federal right is not a rule of law formulated to favor the United States. The Court in the *Clearfield Trust* case was emphatic in pointing out that the United States as the "drawee of commercial paper stands in no different light than any other drawee." 318 U.S. at 369. The Court went on to restate the well-recognized rule set forth in *United States v. National Exchange Bank,* 270 U.S. 527, 534 (1926):

> "'The United States does business on business terms.' It is not excepted from the general rules governing the rights and duties of drawees 'by the largeness of its dealings and its having to employ agents to do what if done by a principal in person would leave no room for doubt.'" 318 U.S. at 369.

The general commercial law now uniformly followed by the states is that an indorsement by any person in the name of a named payee is effective if an agent or

employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no interest in the instrument. Uniform Commercial Code Section 3-405(1)(c).[2] It is not contended that the majority, or unanimous, law of the states is the law of the United States. "[I]t nevertheless stands as a convenient source of reference for fashioning federal rules applicable to these federal questions." *Clearfield Trust Co. v. United States,* 318 U.S. at 367. The then general law merchant was the source of the federal rule accepted in *National Metropolitan Bank v. United States,* 323 U.S. at 457. More recently the Uniform Commercial Code, "well on its way to becoming a truly national law of commerce," has been recognized as an appropriate source for federal law. *See, e.g., United States v. Wegematic Corporation,* 360 F.2d 674, 676 (2d Cir. 1966); *In re Yale Express System, Inc.,* 370 F.2d 433, 437 (2d Cir. 1966). The then general law merchant was adopted in *Metropolitan Bank* because "No persuasive reasons have been suggested to us why it should not be accepted as the general federal rule." 323 U.S. at 457.

There are now persuasive reasons why the general law merchant as it existed in 1942 should no longer be accepted as the general federal rule: that law has been discarded by all of the states; there is now complete uniformity among the states in following a different rule; and the United States now follows a

[2]Louisiana follows the same rule under Uniform Negotiable Instruments Act Section 9(3), as amended.

rule different from the general commercial law. The principles that federal commercial paper should be subject to a uniform rule, and that the United States does business on business terms, are consistent only with the application of the rule now urged. The circumstances to which these principles were applied in *Metropolitan Bank* no longer obtain.

In the absence of an applicable Act of Congress, federal courts must fashion the governing rules. As the lower federal courts have no choice but to follow the decision in *Metropolitan Bank,*[3] the questions raised can only be decided by this Court.

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2. THE DECISION BELOW IS INCONSISTENT WITH THE FEDERAL LAW CONCERNING THE EFFECTIVENESS OF INDORSEMENTS OF TREASURY CHECKS IN IMPOSTOR CASES.

In the closely related "impostor" cases, similar principles have been considered, with the result that the United States is there treated the same as other drawees.

The United States bears the loss resulting from the issuance and delivery of a United States Treasury check to an impostor and negotiation by such impostor upon his indorsement. *See,* for example, *United States v. Bank of America National Trust and Savings Association,* 274 F.2d 366 (9th Cir. 1959), 81 A.L.R.2d 1358; *Atlantic National Bank v.*

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[3]*See,* in addition to the opinions below, *United States v. Philadelphia National Bank,* 304 F.Supp. 955 (E.D. Pa. 1969).

United States, 250 F.2d 114 (5th Cir. 1957); *United States v. Continental-American Bank & Trust Co.,* 175 F.2d 271 (5th Cir. 1949), *cert. denied,* 338 U.S. 870. The reasons for assigning the loss to the government are, if anything stronger in the padded payroll cases than in the impostor cases. Not only is the government defrauded, but it is defrauded by the acts of its own agents or employees. The impostor situation is the same as the forgery situation in the respect that: "What makes the difference between the impostor in law and the forger in law is the intent of the maker, something not to be found on the face or back of the instrument." *United States v. Bank of America,* 274 F.2d at 368. The collecting bank or merchant who accepts the check is in the same position as to each. The negotiability of federal commercial paper should not turn on fine distinctions between the two situations. The federal government should follow the states in recognizing the desirability of applying the same rule to both situations. *Cf. Washington Loan & Trust Co. v. United States,* 134 F.2d at 63.

CONCLUSION

For these reasons, a writ of certiorari should issue to review the judgment and opinion of the Ninth Circuit.

Respectfully submitted,

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May 17, 1971.

(Appendix Follows)

Appendix

United States Court Of Appeals
For The Ninth Circuit

No. 23630

United States of America,
Appellee,
vs.
Bank of America National Trust and Savings Association,
Appellant.

[February 22, 1971]

Appeal from the United States District Court for the Northern District of California

Before: Hamley and Ely, Circuit Judges, and Taylor, District Judge.*

Per Curiam:

The appellant bank cashed six Treasury checks and thereafter warranted the endorsements, presented the checks to the Treasury through the Federal Reserve Bank, and received payment on each of the checks from the Government. The Government subsequently sued the bank to recover the payments and prevailed. The bank appeals.

*Honorable Fred M. Taylor, United States District Judge, Boise, Idaho, sitting by designation.

The issuance of the checks resulted from a fraudulent scheme on the part of the third-party defendants. These two men were enlisted personnel of the United States Navy, attached to the USS Coral Sea and performing duties in the vessel's Disbursing Office. They knew of a shipmate who had recently been discharged from the Navy. One of them obtained the dischargee's identification card and substituted his own photograph thereon. The two schemers then prepared and presented the Treasury checks, payable to the discharged man, to the ship's Disbursing Officer. He signed the checks, and the defrauding seamen, forging the name of the payee and using the false identification card, were able to cash the checks at the bank.

The District Court rested its judgment upon *National Metropolitan Bank v. United States*, 323 U.S. 454 (1945), and we have concluded that we have no choice except to do the same.

The question, of course, is whether the recited circumstances present a situation of legal forgery in the sense that the bank should be required to assume the loss. Under the common law as it existed in 1945, when *Metropolitan* was decided, the question should have been, and was, answered in the affirmative. Since 1945, however, every state in the union, except Louisiana,[1] has adopted the Uniform Commercial Code. Under that Code, the endorsement of a payee's name by a third party is not a legal forgery

[1]Louisiana has adopted an amended version of section 9 of the Uniform Negotiable Instruments Act so that its law, on the issue in question, now coincides with that of the remaining forty-nine states.

in the sense with which we are concerned if an employee of a check's drawer has supplied the drawer with the name of the payee while intending, at the same time, that the payee shall have no interest in the check. Uniform Commercial Code § 3-405(1)(c). The reason for the rule apparently is that the drawer, rather than a nonnegligent bank, should bear the responsibility for faithlessness on the part of its own employees or agents.

Thus, the bank, forcefully and effectively, argues that one of the principal foundations for the Supreme Court's decision in *Metropolitan* has now been undermined. It strengthens this argument by pointing to *Clearfield Trust Co. v. United States,* 318 U.S. 363 (1943), wherein, at 369, the Supreme Court reapplied the expression contained in *United States v. National Exchange Bank,* 270 U.S. 527 (1926):

> " 'The United States does business on business terms.' It is not excepted from the general rules governing the rights and duties of drawees 'by the largeness of its dealings and its having to employ agents to do what if done by a principal in person would leave no room for doubt.' "

All the above notwithstanding, we cannot find that the Supreme Court has itself, since 1945, written anything which might cause us to conclude with reasonable assurance that its *Metropolitan* decision is no longer viable. This being so, we think that *Metropolitan* must now control the disposition of this appeal.

Affirmed.

United States District Court
Northern District of California

No. 47431

Albert C. Wollenberg, District Judge

July 24, 1968

United States of America,
Plaintiff,

vs.

Bank of America National Trust and Savings Association,
Defendant and
Third-Party Plaintiff,

vs.

John Raymond Sherrett and Ronald Wayne Reed,
Third-Party Defendants.

MEMORANDUM OPINION

This is an action by the United States against the Bank of America to recover the proceeds of six Treasury checks presented by the Bank to the plaintiff as issuer and drawee and paid by the Government to the Bank. The Government's theories of recovery are breach of the Bank's expressed and implied warranty of prior endorsement and payment of money

by mutual mistake. The Bank has filed a third party claim against persons who caused the checks to be endorsed and delivered to the Bank.

The facts, as set out in the "Agreed Statement of Facts," prepared by counsel for the Government and bank, are as follows:

"'In 1965 and 1966, third-party defendants Ronald W. Reed and John R. Sherrett were enlisted men in the United States Navy and stationed on board the aircraft carrier USS Coral Sea, which was then in port at San Francisco Bay Naval Shipyard, Hunters Point, California. Both third-party defendants worked in the Disbursing Office. One Gary W. Spiller was also assigned to USS Coral Sea and was discharged January 1, 1966, but actually left the ship December 31, 1965, and was in transit to his point of destination in Bakersfield, California, on January 1, 1966. Spiller had no knowledge of the facts hereinafter stated until he was advised of them by the FBI, subsequent to their occurrence. After Spiller's departure from USS Coral Sea, third-party defendant John R. Sherrett surreptitiously obtained Spiller's identification card and inserted his own photograph in place of Spiller's. Thereafter, third-party defendant Ronald W. Reed made up pay records in favor of Gary W. Spiller, made up the requisite pay receipts and check records, and typed unsigned Treasury checks payable to Gary W. Spiller. The various documents were presented to the Disbursing Officer by either Reed or Sherrett on both regular and special payrolls, and the authorized Disbursing Officer, one

Ensign James Lipsett, signed the checks and gave them back to the man who presented them, to give to Spiller. At all times, Reed and Sherrett intended those events to occur, which did, in fact, occur; that because of the operation of their conspiracy as herein set forth Spiller would not receive any proceeds of the checks. Both Reed and Sherrett were known personally to Lipsett and Lipsett had no reason, from their past conduct, to believe that they had misbehaved in any way in their duties. It was their regular and authorized job to prepare the documents described in the regular course of business for regular and special payroll; said documents comprised all the documentation necessary for the issuance of said pay checks. At the signing of each and all of the checks, Ensign Lipsett intended to pay, on behalf of the Government, a definite living person then stationed on board USS Coral Sea to whom the money was lawfully due. The individual presenting the checks, either Reed or Sherrett, represented to Lipsett on the occasion of signing some of the checks the Spiller had reenlisted. Spiller was not known personally to Lipsett; however, on the regular payroll the name appeared with other names personally known to Lipsett. Had Lipsett known the true facts in this matter, he would not have signed the checks. The checks thus issued were dated, numbered and in the amounts as follows:

Date	*Amount*	*Number*
4 Feb 1966	$ 552.00	35578
15 Feb 1966	181.00	35674
21 Feb 1966	1305.00	35820
2 Mar 1966	1452.00	36069
15 Mar 1966	850.00	36219
22 Mar 1966	2332.00	36311

As to those checks presented to Lipsett by Reed, third-party defendant Reed from time to time gave the checks to third-party defendant Sherrett, following their issuance. Third-party defendant Sherrett took all the checks and presented them at various times at various branches of defendant Bank of America National Trust and Savings Association, after signing the endorsement of Gary W. Spiller thereon. On each occasion the identification card was exhibited to the tellers, who did not observe any reason to suspect Sherrett. Upon receipt of payment, third-party defendant Sherrett split the proceeds with third-party defendant Ronald Reed. The defendant Bank of America endorsed each and all of said checks with an express written guaranty of prior endorsements and presented them to the Treasury through the Federal Reserve Bank. Payment was made by the Government on each of said checks to the defendant Bank of America. Said payment was made without knowledge of the unauthorized signature of Gary W. Spiller; if said knowledge were had by the Government, payment would not have been made. If payment had not been made, the Bank would have made claim against the Government, alleging itself to be a holder in due course.

"Criminal action No. 40987 was brought in the above-entitled court against third-party defendants Ronald W. Reed and John R. Sherrett and both were convicted upon their please of guilty to uttering and publishing as true a falsely made Treasury check. Sentence was suspended as to both defendants, and both were placed on five years probation and ordered to make restitution in the sum of $1166.00, individually. At the present date, third-party defendant Ronald W. Reed has paid only $80.00 on his restitution. Demand was made upon the defendant Bank of America to pay the United States of America the sum of $6672.00 on account of the presentment and payment by the Government of the checks herein described on May 4, 1967, prior to the filing of the present action."

The issue before this Court is whether a federal court should adopt by analogy as "federal Law" Section 3—405(1)(c)[1] of the Uniform Commercial Code, adopted by all but one of the states,[2] in lieu of the "federal law" established by United States Supreme Court in National Metropolitan Bank v. United States, 323 U.S. 454, 65 S.Ct. 354, 89 L.Ed. 383 (1945).

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[1]U.C.C., Section 3405(1)(c) provides:

"(1) An endorsement by any person in the name of a named payee is effective if • • • (c) An agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest."

[2]The Code has also been adopted in the District of Columbia and the Virgin Islands. Louisiana, the only state which does not have the U.C.C. does have the amended version of Section 9 of the Uniform Negotiable Instruments Act, which is similar to the U.C.C.

In the *Metropolitan Bank* case, a government employee drew up travel and pay vouchers in the name of living military personnel and presented Treasury checks conforming to the vouchers to the disbursing officer for signature. The employee then took the checks, signed the names of the payees as endorsement, signed his name as second endorsement and obtained the proceeds. The bank then presented the checks to the government, who paid the Bank the amount of the checks. The Supreme Court held, under these facts, that its holding in Clearfield Trust Co. v. United States, 318 U.S. 363, 63 S.Ct. 573, 87 L.Ed. 838 (1943) that "[b]reach of [the warranty of prior endorsements] * * * by presenting a check on which the payee's signature is a forgery, gives the government a right to recover from the guarantor when payment is made" (323 U.S. at 456, 65 S.Ct. at 355) controls the outcome of the case. As to the Bank's contention that the affirmative negligence of the Government in failing to discover the fraud ought to preclude relief, the Court applied the general law merchant, which rejected this defense. It noted that this general rule "has been almost unanimously accepted by State and federal courts." It continued, "No persuasive reasons have been suggested to us why it should not be accepted as the general federal rule." 323 U.S. at 457, 65 S.Ct. at 356.

Defendant does not seriously urge that the *Metropolitan Bank* case does not apply to the instant case. What defendant suggests is that the meaning of the *Metropolitan Bank* case is that federal courts must

look to the general commercial law at the time of the transaction in fashioning a "federal law." Its argument, simply stated, is that now that 49 states have adopted Section 3—405(1)(c) of the Uniform Commercial Code, that law is the general commercial law and should be followed now by this Court in fashioning a federal rule. Clearly, defendant does not ask that this Court adopt the U.C.C. as such, but rather asks that this Court follow the U.C.C. by analogy.

Before evaluating defendant's argument, it is necessary to place the *Clearfield Trust* case in its historical perspective. Prior to that decision, the federal courts in cases involving federal commercial paper followed state law under apparent authority of Erie R. Co. v. Tompkins, 304 U.S. 64, 58 S.Ct. 817, 82 L.Ed. 1188 (1938). See e. g., United States v. Bank of America, 47 F.Supp. 279 (N.D. Cal. 1942). The District Court in the *Clearfield Trust* case had in fact applied the law of Pennsylvania which was to the effect that if the issuer (there, the Government) of the check unreasonably delayed in giving notice of the forgery to the bank, prejudice to the bank would be presumed, and recovery by the Government would be precluded. The Supreme Court held that *Erie* did not apply to cases involving the rights and duties of the United States on its own commercial paper, stating:

> "The rights and duties of the United States on commercial paper which it issues are governed by federal rather than local law. When the United States disburses its funds or pays its debts, it is exercising a constitutional function or power. * * * In absence of an applicable Act of Congress it is

for the federal courts to fashion the governing rule of law according to their own standards." Clearfield Trust Co. v. United States, 318 U.S. at 366-367, 63 S.Ct. at 575.

The rationale for applying a federal rule in cases involving commercial paper of the United States was succinctly stated by the Court in the following quoted portion from its opinion, 318 U.S. at 367, 63 S.Ct. at 575:

> "In our choice of the applicable federal rule we have occasionally selected state law. See Royal Indemnity Co. v. United States, supra, [313 U.S. 289, 61 S.Ct. 995, 85 L.Ed. 1361.] But reasons which may make state law at times the appropriate federal rule are singularly inappropriate here. The issuance of commercial paper by the United States is on a vast scale and transactions in that paper from issuance to payment will commonly occur in several states. The application of state law, even without the conflict of laws rules of the forum, would subject the rights and duties of the United States to exceptional uncertainty. It would lead to great diversity in results by making identical transactions subject to the vagaries of the laws of the several states. The desirability of a uniform rule is plain. *And while the federal law merchant developed for about a century under the regime of* Swift v. Tyson, 16 Pet. 1, 10 L.Ed. 865, *represented general commercial law rather than a choice of a federal rule designed to protect a federal right, it nevertheless stands as a convenient source of reference for fashioning federal rules applicable to these federal questions.* [Emphasis supplied].

The Court then went on to discuss the various *federal* cases in this area, and applied a rule of law which would preclude the Government from recovery only if actual prejudice were shown to have resulted to the bank from its delay in giving notice. United States v. National Exchange Bank of Providence, 214 U.S. 302, 29 S.Ct. 665, 53 L.Ed. 1006 (1909).

It is quite clear that the Supreme Court in *Clearfield* was pointing the federal courts in a new direction. Had it only held that *Erie* was inapplicable, the federal courts would have then fallen back on the blind precedents set during the reign of Swift v. Tyson, 16 Pet. 1, 41 U.S. 1, 10 L.Ed. 865 (1842). But the Court went further when it spoke for the first time of the duty of the federal courts to *choose* "a federal rule *designed* to protect a federal right." 318 U.S. at 367, 63 S.Ct. at 575. [Emphasis supplied]. A "convenient source" for this rule would be the "general commercial law" established in the federal cases. 318 U.S. at 367, 63 S.Ct. 573.

Two years later, the *Metropolitan Bank* case was decided, which affirmed the principles set down in *Clearfield Trust*. In light of *Clearfield*, the holding in the *Metropolitan Bank* case could be interpreted as a *choice* by the Court of a federal rule "designed to protect a federal right", rather than as the adoption by the federal courts of the law existing in the majority of state jurisdictions at that time. However, defendant would have us believe that the holding in the *Metropolitan Bank* case was simply one in which the Court followed the "majority rule", and now that the "majority rule" has been changed by the U.C.C.,

this Court ought to feel free to adopt that body of law. Defendant apparently finds support for its position in the Court's statement that the rule followed in the *Metropolitan Bank* case had "been unanimously accepted by State and federal courts." 323 U.S. at 457, 65 S.Ct. at 356.

The language cited above does not lend full support to defendant's argument that in fashioning a federal rule, the only consideration of a federal court is what a majority of the states have adopted. The *Clearfield Trust* doctrine gives a federal court the added function of developing a body of law consonant with those interests which are uniquely federal. *Banco Nacional de Cuba v. Sabbatino,* 376 U.S. 398, 426, 84 S.Ct. 923, 11 L.Ed.2d 804 (1964). Hence, the Court in the *Metropolitan Bank* case (the same Court which rendered the *Clearfield Trust* decision two years earlier) was, in addition to citing the majority rule as *support* for its decision, also defining the federal interest in protecting its rights in commercial paper which it issued.

It must be made clear that one of the factors which concerned the Court in *Clearfield* and *Metropolitan Bank* is not present in the instant situation. In both those cases, the Court was concerned with the adverse effect on the federal government of applying different state rules to the same federal transactions. Hence, it stressed the need for uniformity as one reason for adopting a federal rule. Here, section 3—405(1)(c) of the U.C.C. has been adopted by 49 of the 50 states, and its principles are followed by the lone dissenter.[3]

[3]See Note 2.

If this Court should decide to adopt by analogy the rule announced by the U.C.C., there would be no problem with regard to different rules applying in each jurisdiction, although as the Government points out, the effect of different federal courts applying either the *Metropolitan* holding or the U.C.C. would be disastrous on the quest for uniformity within the federal system.

While the need for uniformity will be met with the adoption of either body of law, this Court still has the duty of determining the federal interest in protecting the government's rights in its commercial paper. We think that the *Clearfield* and *Metropolitan Bank* Court did just that when it determined that the Government should not be precluded from recovering from a presenting bank notwithstanding its affirmative negligence. That Court was well aware of the rule of law which defendant has thrust upon us as is clear by the cases cited in the National Metropolitan Bank's brief. See National Metropolitan Bank v. United States, 89 L.Ed., at 384. Yet, it chose, as was dictated by *Clearfield Trust,* that the federal interest was best served by allowing the Government to recover. Because the several states have adopted a different rule does not mean that the federal interest, as announced in the *Metropolitan Bank* case, has been since diluted. To the contrary, the federal government is not in the same position as a private person with respect to its control over its employees. The whole rationale behind Section 3—405(1)(c) of the U.C.C., as stated in the Official Comments thereto, is "that the

loss should fall upon the employer as a risk of his business enterprise rather than upon the subsequent holder or drawee." The Comment further states: "The reasons are that the employer is normally in a better position to prevent such forgeries by reasonable care in the selection or supervision of his employees, or, if he is not, is at least in a better position to cover the loss by fidelity insurance; and that the cost of such insurance is properly an expense of his business rather than of the business of the holder or drawee." Comment 4 to Section 3—405(1)(c), U.C.C.

As the government points out,

> "Reed and Sherrett were enlisted men in the Navy. The Navy is not a business enterprise but is required to be maintained in the interest of national security. Non-commissioned personnel are enlisted into the Navy on a far different basis, and with less opportunity for care in selection, than payroll personnel in a private corporation. Because of the volume of enlisted personnel in the Navy and the rapid turnover in positions, it is not feasible for the Government to maintain character investigatory systems or to cover the loss by fidelity insurance as suggested in the Code commentary. * * * It may also be observed that the Government also operates far less profitably than nearly all presenting banks. The business risk rationale is not in point; public moneys need protection more than the presenting bank's assets." Opening Brief for the United States, p. 7.

This Court agrees with the Government's statement. The Government, especially with respect to military

personnel, cannot be expected to exercise the same control as private enterprise over its employees. It is noteworthy that in both *Clearfield* and *Metropolitan Bank*, the employees involved were civilian rather than military. If, as both cases impliedly hold, the Government cannot be expected to maintain any meaningful control over its civilian employees, it can hardly be said that it must do so regarding men in the military.

In rejecting defendant's basic contention for the above-stated reasons, this Court is also mindful of its role as an inferior court and of the possible conflicts which would be created among the various Circuits if it accepted defendant's argument, which would have a profound effect on the uniformity desired in this particular area. While there may be some doubt as to the actual reasons for the Supreme Court's rejection of defendant's basic theories in the *Clearfield* and *Metropolitan Bank* cases, only today's Supreme Court can give us the answer and at the same time preserve the uniformity which has existed since *Clearfield*.

Accordingly, for the reasons mentioned in this opinion, plaintiff is entitled to recover against defendant the amount as prayed for with interest. Plaintiff is to have its costs of suit herein, and to prepare an appropriate decree. This opinion shall constitute findings of fact and conclusions of law as is required by the Rules.

In the United States District Court for the Northern District of California

Civil No. 47431

United States of America,
Plaintiff,

vs.

Bank of America National Trust and Savings Association,
Defendant and Third-Party Plaintiff,

vs.

John Raymond Sherrett and Ronald Wayne Reed,
Third-Party Defendants.

STIPULATION OF ADDITIONAL AGREED FACTS

It Is Stipulated by and between the parties hereto through their respective attorneys that the face amounts of Checks No. 35578 in the sum of $552.00; No. 35674 in the sum of $181.00; No. 35820 in the sum of $1,305.00; No. 36069 in the sum of $1,452.00; and No. 36219 in the sum of $850.00, in the total sum of $4,340.00 were paid by plaintiff to defendant not later than April 22, 1966, on account of said check and that the face amount of check No. 36311 in the sum of $2,332.00 was paid by plaintiff to defendant no later than May 4, 1966 on account of said check.

It is further stipulated that the present amount paid by third-party defendant, Ronald W. Reed on his restitution order is $100.00 and the amount paid by third-party defendant, John R. Sherrett on his restitution order is nil.

It is further stipulated that the probation order with regard to third-party defendant, John R. Sherrett, in Criminal Action N. 40987 orders restitution to be paid in such amounts as may be fixed by the Probation Office, and the Probation Office set the figure at $1166.00.

It is further stipulated that the restitution order as to the third-party defendant, Ronald W. Reed and the restitution order as to the third-party defendant, John R. Sherrett both order restitution through the Probation Office only, and no other person to whom restitution is to be made is mentioned in either order.

Dated: May 7, 1968.

Cecil F. Poole.
United States Attorney

By Peter V. Shackter
Assistant United States Attorney

Theodore Sachsman, Attorney for
Bank of America National Trust
and Savings Association

Original filed May 7, 1968,
Clerk, U.S. Dist. Court, San Francisco.

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No. 1722

In the Supreme Court of the United States

OCTOBER TERM, 1970

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

ERWIN N. GRISWOLD,
Solicitor General,
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QUESTION PRESENTED

Whether the United States may recover the value of Treasury checks paid upon the forged endorsements of the payee from a presenting bank, where government employees were responsible for the forgeries.

STATUTE AND REGULATIONS INVOLVED

Section 3–405 of the Uniform Commercial Code provides in part:

> (1) An indorsement by any person in the name of a named payee is effective if
>
> * * * * *
>
> (c) an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest [in the instrument].

Title 31, Part 360 of the Code of Federal Regulations provides in part:

> § 360.4 Guaranty of indorsements.
>
> The presenting bank and the indorsers of a check presented to the Treasurer for payment are deemed to guarantee to the Treasurer that all prior indorsements are genuine, whether or not an express guaranty is placed on the check. When the first indorsement has been made by the one other than the payee personally, the presenting bank and the indorsers are deemed to guarantee to the Treasurer, in addition to other warranties, that the person who so indorsed had unqualified capacity and authority to indorse the check in behalf of the payee.

§ 360.5 Reclamation of amounts of paid checks.

The Treasurer shall have the right to demand refund from the presenting bank of the amount of a paid check if after payment the check is found to bear a forged or unauthorized indorsement or an indorsement by another for a deceased payee where the right to the proceeds of such check terminated upon the death of the payee, or to contain any other material defect or alteration which was not discovered upon first examination. If refund is not made, the Treasurer shall take such action against the proper parties as may be necessary to protect the interests of the United States.

STATEMENT

The United States sued the Bank of America National Trust and Savings Association for breach of a contract of guaranteee and to recover money paid by mistake. The district court held for the government on the basis of *National Metropolitan Bank* v. *United States,* 323 U.S. 454, which is factually identical, and because of paramount considerations of federal policy (Pet. App. viii–xvi).[1] The court of appeals unanimously affirmed on the ground that *Metropolitan* was dispositive.

The relevant facts were stipulated. At the pertinent times in 1965 and 1966, Sherrett and Reed were enlisted men working in a Navy disbursing office. Early in 1966, they obtained the identification card of one Spiller, who had been discharged from the Navy on

[1] The district court also entered judgment for the Bank on its uncontested third-party complaint against Sherrett and Reed, the culpable government employees (Pet. 6).

CITATIONS—Continued

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In the Supreme Court of the United States

OCTOBER TERM, 1970

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UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the United States District Court for the Northern District of California (Pet. App. iv–xvi) is reported at 288 F. Supp. 343. The opinion of the United States Court of Appeals for the Ninth Circuit (Pet. App. i–iii) is not yet reported.

JURISDICTION

The judgment of the court of appeals was entered on February 22, 1971. The petition for a writ of certiorari was filed on May 19, 1971. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

429-792—71——1

January 1, 1966. Sherrett substituted his picture for that of Spiller. Reed made up pay records, pay receipts and check records in Spiller's name, and typed unsigned Treasury checks payable to Spiller. They then presented these documents to the disbursing officer. The latter, having no knowledge of any wrongdoing and no reason to suspect it, signed six checks, totaling $6,672 over a six-week period. Each check was returned to Sherrett or Reed for delivery to Spiller.

Sherrett took the checks to various branches of the Bank. In each instance, he signed Spiller's name and showed the altered identification. The Bank cashed each of the checks, believing him to be Spiller. The record does not indicate whether other identification was rquested and the signature was not verified.

The Bank indorsed each of the checks with an express guaranty of prior indorsements and presented them to the Treasury through the appropriate Federal Reserve Bank. Each was paid without knowledge on the part of the Treasury of the unauthorized signatures. Shortly thereafter, the forgeries were discovered. Sherrett and Reed were arrested and subsequently convicted.[2]

ARGUMENT

Petitioner concedes that this case is factually similar to *National Metropolitan Bank* v. *United States*, 323 U.S. 454, but argues (Pet. 7–10) that *Metropolitan* is no longer viable because the decision there was

[2] Some reimbursement was made by Reed, thus reducing the government's claim.

based upon the then-prevailing principle of commercial law favoring the drawer of the check while commercial law now favors the bank (Uniform Commercial Code, Section 3–405). Contrary to petitioner's contention, however, *Metropolitan* rested not only upon general commercial law, but also on federal policy considerations which are still valid today. The decision below is, in any event, of limited significance in view of the adoption, effective in October 1967, of a Treasury regulation explicitly making the drawee bank responsible in instances of forged indorsements. (31 C.F.R. 360.5). Review by this Court is therefore not warranted.

1. *Metropolitan* also involved the government's attempt to obtain reimbursement for payments to a bank which had, in good faith, presented checks which had been forged by military personnel. The Court, sustaining the government's claim, expressly rejected the bank's argument that the loss should fall on the government since it was caused by "negligence of the government's administrative officers in detecting the fraud of its clerk * * *." 323 U.S. at 456. The Court stated that this defense had been rejected in *United States* v. *National Exchange Bank,* 214 U.S. 302, where the Court had been "applying the general law merchant * * *." 323 U.S. at 457. It concluded that "[n]o persuasive reasons have been suggested to us why it should not be accepted as the general federal rule." *Ibid.* The Court in *Metropolitan* pointed out that most state courts had accepted the rule urged by the government, although it noted *Washington Loan & Trust Co.* v. *United States,* 134 F. 2d 59 (C.A. D.C.),

which had discussed the practice of several states to the contrary. *Ibid.*

The Court did not, however, rest its opinion solely on the prevailing state law. It stressed Treasury regulations which require a blanket and absolute guarantee of prior endorsements and discussed their purpose. 323 U.S. at 458 (emphasis added):

> This guaranty [set out in the regulation] was a protection which the government sought not only as to checks which were issued in due course for a valuable consideration, but as to checks which might have been irregularly issued. That the administrative officers failed fully to perform their duty is no reason why the government should be deprived of the advantage of a guarantee *independently made by one who was not under compulsion of any kind to make it.* No equitable principles require that one who, *for his own reasons,* guarantees a payee's signature after issuance of a check, shall be relieved of his *voluntarily assumed obligation* because others who owed the government obligations had previously defaulted in their obligations.

The regulation (now 31 C.F.R. 360.4) is still in existence. Indeed, the Treasury Department, as we note below, pp. 9–10, promulgated another regulation (31 C.F.R. 360.5) subsequent to *Metropolitan* expressly codifying the decision in that case.[3]

[3] While the new regulation does not apply to the particular transactions involved here, it does represent a clear statement of the continuing federal policy concerning the government's rights to be protected by a presenting bank's guaranty of prior indorsements and to recover when that guaranty is broken.

The considerations of the policy which the *Metropolitan* decision reflects are still pertinent today. Comparing the respective positions of banks and the government, then as now, reveals cogent reasons for placing the risk of payment of forged checks upon banks, even though commercial law now generally places that burden upon business employers.

Banks have an opportunity to guard against paying such checks. As a practical matter, most persons seeking to endorse a forged check will be persons who are not customers or otherwise known to the bank. In these cases, the bank can minimize its risks by requiring thorough verification of signature or additional identification from such strangers. As a last resort, the bank can simply refuse to cash a check presented by a stranger.

The United States, on the other hand, is not a typical business employer. The government is not a profit-making enterprise, nor is it "normally in a better position to prevent * * * forgeries" by selecting better employees. U.C.C. § 3–405, comment 4. We are informed by the Treasury Department that in fiscal year 1968 approximately 574,000,000 checks were drawn on the Treasury of the United States. See also Annual Report of the Secretary of the Treasury, 1968, p. 89. This is twice the number drawn yearly at the time of the decision in *Metropolitan*. Brief for the United States, No. 161, Oct. Term, 1944, p. 21. Many thousands of persons take part in the preparation and disbursement of these government checks. Many are not hired for the purpose of disbursing government funds,

but are Armed Forces personnel serving short terms in government "employment," as were Sherrett and Reed here. The costs of bonding all employees or of making more extensive character investigations would be significant. And those costs would be charges on the public treasury, borne by the taxpayers, rather than a cost of doing business, borne ultimately by stockholders.

Uniquely federal interests thus justify the retention of the federal rule, regardless of the change in state law.[4] In *Clearfield Trust* v. *United States,* 318 U.S. 363, the Court recognized that "[t]he rights and duties of the United States on commercial paper which it issues are governed by federal rather than local law," and that Treasury regulations covered almost every aspect of its negotiability. 318 U.S. at 366 & n. 2. The same is true today. See 31 C.F.R. Part 360; 5 U.S.C. 301; see also 18 U.S.C. 286, 287, 471. And federal statutes and case law protect the Treasury in many other areas where state law would give precedence to other parties. *E.g.,* 31 U.S.C. 191–192 (government debts to be first satisfied in insolvency situations); *United States* v. *City of New Britain,* 347 U.S. 81, 85.

2. Petitioner does not contend that the decision below, in continuing to follow *Metropolitan,* directly conflicts with that of any other circuit. Indeed, the

[4] Although thirty-eight states had adopted the rule urged by the Bank as of 1963, this Court still reaffirmed the proposition that "federal law applies * * * in a choice of substantive law * * * in cases involving rights and obligations arising on commercial paper issued by the United States," citing the *Metropolitan* decision. *International Assn. of Machinists* v. *Central Airlines, Inc.*, 372 U.S. 682, 693, n. 17.

Fifth Circuit applied *Metropolitan* in 1957, by which time seventeen states had adopted a rule favoring the bank. *Atlantic National Bank of Jacksonville* v. *United States,* 250 F. 2d 114 (C.A. 5). Petitioner does argue, however (Pet. 10–11), that the decision below is essentially inconsistent with decisions of several federal courts which have refused to extend the *Metropolitan* rule to the "imposter" situation involving fictitious payees. See *United States* v. *Bank of America National Trust and Savings Association,* 274 F. 2d 366 (C.A. 9); *Atlantic National Bank of Jacksonville* v. *United States, supra.* The alleged inconsistency is of no consequence in this context, for the courts below correctly applied the *Metropolitan* rule to forgers here. Whether that rule also should be applied to impostor situations is, of course, not presented in this case.

3. The prospective importance of the decision below has been considerably reduced by the promulgation of a new Treasury regulation. All the checks in question here were paid in 1966 (Pet. App. xvii). In October 1967, a Treasury regulation was adopted expressly codifying the holding in *Metropolitan:*

> § 360.5 Reclamation of amounts of paid checks.
>
> The Treasurer shall have the right to demand refund from the presenting bank of the amount of a paid check if after payment the check is found to bear a forged or unauthorized indorsement * * *. If refund is not made, the Treasurer shall take such action against the proper parties as may be necessary to protect the interests of the United States.

In our view, this regulation will control and dispose of virtually all future cases of a forged and unauthorized indorsement. Cf. *United States* v. *Shimer*, 367 U.S. 374, 377.

CONCLUSION

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1971

No. 70-180

BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, *Petitioner,*

vs.

UNITED STATES OF AMERICA, *Respondent.*

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

REPLY BRIEF OF BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION

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REPLY BRIEF OF BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION

OPINION BELOW

The opinion of the Court of Appeals (Pet. App. i-iii) is reported, 438 F.2d 1213 (1971).

INTRODUCTION

Bank of America presents this Reply Brief in answer to the arguments set forth by the United States.*

ARGUMENT

1. RESPONDENT MISCONSTRUES THE QUESTION PRESENTED

Respondent argues (R.B. 2) that the question presented is:

> "Whether the United States may recover the value of Treasury checks paid upon the forged endorsements of the payee from a presenting bank, where government employees were responsible for the forgeries."

Petitioner contends, and the Court of Appeals agrees, that the question presented is whether the recited circumstances present a situation of legal forgery, or whether the indorsements are effective. Pet. 2; Pet. App. i, ii; *see* Uniform Commercial Code §3-405(1)(c).

---

2. THE TREASURY REGULATIONS RELIED UPON BY RESPONDENT DO NOT APPLY

The United States has set forth the argument that the Treasury Regulations cited (31 C.F.R. §§360.4 and 360.5, the latter such section being promulgated subsequent to the events giving rise to the instant

---

erratum: The fourth paragraph on page 6 of the Petition should read, "The trial court sitting *without* a jury had jurisdiction under 28 U.S.C.A. §1345."

action) evidence a federal rule of law inconsistent with the rule established by U.C.C. §3-405(1)(c). Bank of America contends that such an assertion merely begs the question.

31 C.F.R. §§360.4 and 360.5 do no more than provide that a presenting bank is deemed to guarantee prior indorsements, and that the Treasurer may demand refund of the amount of a check paid on a forged indorsement from the presenting bank. R.B. 2, 3. These regulations do not reach the question of whether indorsements in padded payroll cases are forgeries.

Under state law there is a similar right of recourse against previous indorsers and the collecting and presenting banks. Under U.C.C. §§3-417 and 4-207 indorsers, collecting and presenting banks are required to warrant to their transferee that they have good title to the instrument presented and that all signatures are genuine or authorized. This is essentially what the cited Treasury Regulations provide. Thus, the state law merchant is in complete accord with the Treasury Regulations.

Notwithstanding the warranty as to genuineness of indorsements which is required under U.C.C. §§3-417 and 4-207 (and under 31 C.F.R. §§360.4 and 360.5), the general law merchant, as codified throughout the state jurisdictions, provides that any signature in the name of the named payee in the circumstances found here is "effective." U.C.C. 3-405(1)(c). In the case of such an indorsement, *as a matter of law the signature cannot be a forgery, no matter who signs the name*

of the payee. Since this latter rule is neither codified by Treasury Regulation, nor is it negatived by a contrary regulation, recourse still must be had to the federal law merchant. It remains for this Court to fashion the governing rules.

CONCLUSION

For the reasons set forth herein and in Bank of America's Petition, a writ of certiorari should issue to review the judgment and opinion of the Ninth Circuit.

Respectfully submitted,

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Dated, September 28, 1971.